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No. 94-1183

In the Supreme Court of the United States

OCTOBER TERM, 1994

NORAM ENERGY CORPORATION, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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QUESTION PRESENTED

Whether collateral estoppel bars petitioner from asserting that the recoverable portions of its cushion gas and line pack gas are subject to the allowance for depreciation for federal income tax purposes.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-14a) is reported at 37 F.3d 621. The Court of Federal Claims issued two opinions. The first (Pet. App. 15a-32a) is reported at 27 Fed. Cl. 226. The second (Pet. App. 33a-38a) is unreported.

JURISDICTION

The judgment of the court of appeals was entered on October 4, 1994. The petition for a writ of certiorari was filed on December 30, 1994. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Petitioner operates a natural gas pipeline system through which it transmits natural gas for sale to customers in Arkansas, Louisiana, Kansas, Oklahoma and Texas (Pet. App. 3a-5a). Petitioner also operates an underground gas reservoir known as the Chiles Dome in which it temporarily stores gas for future sales (*ibid.*).

In order for the Chiles Dome facility to operate at peak efficiency, petitioner maintained a constant quantity of gas, known as "cushion gas," within the reservoir (Pet. App. 3a). Similarly, in order for petitioner's pipeline system to operate efficiently, it was necessary to maintain a constant quantity of gas, known as "line pack gas," within the system (*id.* at 4a-5a). The gas that is referred to as "cushion gas" and "line pack gas" is physically indistinguishable from the natural gas delivered to petitioner's customers (*id.* at 17a). The terms simply refer to the quantity of gas required to maintain the optimal pressure in the reservoir and pipeline system (*ibid.*).

Cushion gas and line pack gas are largely recoverable; they can be withdrawn and sold upon abandonment of the reservoir or the pipeline system (Pet. App. 3a). The portion of cushion and line pack gas that cannot economically be withdrawn is referred to as "nonrecoverable" gas.

2. In 1980, petitioner purchased gas for injection into the Chiles Dome reservoir as cushion gas (Pet. App. 3a). Petitioner claimed an investment tax credit under 26 U.S.C. 38 for the entire cost of that cushion gas (Pet. App. 3a-4a). When the Internal Revenue Service disallowed the claimed credit, petitioner paid the resulting deficiency and sued for a refund in the United

States District Court for the Western District of Louisiana (*id.* at 4a).

The district court granted summary judgment for petitioner, but the court of appeals reversed. *Arkla, Inc.* v. *United States*, 765 F.2d 487 (5th Cir. 1985) (*Arkla I*), cert. denied, 475 U.S. 1064 (1986).[1] The court noted that the investment tax credit is available only for depreciable property. *Id.* at 489. The recoverable portion of petitioner's cushion gas was not depreciable, however, because it would remain unchanged in the reservoir for an indefinite period of time and could be retrieved and sold when the reservoir was closed. *Id.* at 490. The investment tax credit was therefore not applicable to petitioner's cushion gas. *Ibid.*

3. In 1981, petitioner purchased additional cushion gas for the Chiles Dome reservoir (Pet. App. 4a). Petitioner claimed both the investment tax credit under 26 U.S.C. 38 and a deduction for depreciation under 26 U.S.C. 168 for the recoverable and nonrecoverable portions of that cushion gas (Pet. App. 4a). Petitioner also claimed the investment tax credit and a depreciation deduction for line pack gas it purchased and placed in service in 1981 (*id.* at 5a).

When the IRS disallowed the claimed investment tax credits and depreciation deductions, petitioner paid the deficiencies and filed suit for refund in the Court of Federal Claims (Pet. App. 4a). That court held that petitioner was entitled to a refund for the portion of the disputed claim that related to the *non*recoverable cushion and line pack gas (*ibid.*). The court further held that the decision in *Arkla I* collaterally estopped petitioner from claiming an investment tax credit and

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[1] Petitioner was named "Arkla, Inc." prior to May of 1994 (Pet. ii).

depreciation deduction for the recoverable portion of its cushion gas (Pet. App. 4a). On the merits, the court also held that petitioner was not entitled to the investment tax credit or a depreciation deduction for the recoverable portion of its line pack gas (*id.* at 5a).

4. The court of appeals affirmed. The court agreed with the Court of Federal Claims that collateral estoppel barred petitioner from relitigating the question whether its recoverable cushion gas was depreciable (Pet. App. 6a-12a). The court also held that petitioner was collaterally estopped from arguing that its line pack gas was depreciable on the ground that there was no material factual difference between line pack gas and cushion gas (*id.* at 12a-13a).

ARGUMENT

The decision of the court of appeals is correct and does not conflict with any decision of this Court or any other court of appeals. Further review is therefore not warranted.

The doctrine of collateral estoppel bars parties to a prior lawsuit from relitigating any issue that was actually and necessarily determined by a court of competent jurisdiction in the prior suit. *Parklane Hosiery Co.* v. *Shore*, 439 U.S. 322, 326 n.5 (1979). The doctrine serves "the dual purpose of protecting litigants from the burden of relitigating an identical issue with the same party or his privy and of promoting judicial economy by preventing needless litigation." *Id.* at 326. Collateral estoppel will apply if (i) the party against whom estoppel is asserted was a party in the prior action, or a privy to a party, (ii) the issue sought to be relitigated is identical to the one decided in the prior action, (iii) the controlling facts and legal principles remain unchanged, and (iv) no special circumstances

warrant an exception to the otherwise applicable rules of preclusion. *United States* v. *Stauffer Chemical Co.*, 464 U.S. 165, 169 (1984); *Montana* v. *United States*, 440 U.S. 147, 155 (1979).

a. In *Arkla I*, petitioner claimed that it was entitled to the investment tax credit for the recoverable portion of the cushion gas it acquired and injected into the Chiles Dome facility in 1980. The investment tax credit is allowable only for property that is subject to the allowance for depreciation. 26 U.S.C. 46, 48. Property is depreciable only if, among other things, it is subject to exhaustion, wear and tear and has a determinable useful life. 26 U.S.C. 167(a). See *Newark Morning Ledger Co.* v. *United States*, 113 S. Ct. 1670, 1680-1681 (1993) (property is depreciable only if it "has a value that wastes over an ascertainable period of time"). In *Arkla I*, the Fifth Circuit held that petitioner's recoverable cushion gas is not depreciable because it will not waste and, at the end of the storage facility's useful life, it "will be available for sale or other use, with its general utility and value undiminished in any fashion." 765 F.2d at 490.

The parties and the issue in the instant case are identical to those in *Arkla I*. Although in *Arkla I* petitioner claimed entitlement only to the investment tax credit, while here it claims both the investment tax credit and depreciation deductions, both of those tax benefits are available only for property that is subject to exhaustion, wear and tear and has an ascertainable useful life. In *Arkla I*, the recoverable portions of petitioner's gas were held not to meet that standard. 765 F.2d at 490.

b. The controlling facts and legal principles involved in this case are identical to those involved in *Arkla I*. The two factual differences between this case and *Arkla I* are not material: (i) This case concerns cushion gas

petitioner placed in service in 1981, while *Arkla I* involved cushion gas placed in service in 1980. The decision in *Arkla I*, however, did not turn on the year in which the non-depreciable gas was placed in service. (ii) This case, unlike *Arkla I*, involves "line pack gas" as well as "cushion gas." As the court of appeals noted (Pet. App. 12a), however, line pack gas is "functionally equivalent" to cushion gas for both are used merely to maintain an optimal constant pressure in a gas facility. The controlling fact with regard to line pack gas, as with cushion gas, is that the recoverable portion of that gas is not a wasting asset and has no ascertainable useful life (*id.* at 12a-13a).

c. No change in the controlling legal principles occurred between the 1980 and 1981 tax years. Both *Arkla I* and this case turn on whether petitioner's recoverable gas is depreciable, and there was no change in the definition of depreciable property between 1980 and 1981. Petitioner argues (Pet. 16) that a change in the controlling legal principles was effected by the addition of Section 168 to the Internal Revenue Code, effective for property placed in service after December 31, 1980. Petitioner alludes to 26 U.S.C. 168(f)(9) (1982), under which salvage value is not to be considered in determining the amount of depreciation deductions. That provision affects only the calculation of the deduction when applicable; it does not alter the definition of depreciable property as property that is subject to exhaustion, wear and tear and that has a determinable useful life. Petitioner's line pack and cushion gas do not qualify under that definition (Pet. App. 12a-13a).[2]

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[2] Petitioner claims (Pet. 17) that collateral estoppel should not be applied because *Arkla I* itself effected a change in law. The contention that the earlier decision was incorrect (or otherwise not

d. Petitioner errs in contending (Pet. 6-9) that the decision in this case conflicts with this Court's decisions in *Commissioner* v. *Sunnen*, 333 U.S. 591 (1948), and *Limbach* v. *Hooven & Allison Co.*, 466 U.S. 353 (1984). In those cases, the Court held that collateral estoppel would not apply where different tax years are in issue if there has been an intervening change in the law. 466 U.S. at 362. See also *Montana* v. *United States*, 440 U.S. at 161 (collateral estoppel did not apply in *Sunnen* because "there had been a 'significant change in the legal climate'"). A corollary to this rule is that, so long as the controlling legal principles remain unchanged, collateral estoppel will apply even though—as in this case—a subsequent lawsuit places a different tax year in issue.

e. Finally, petitioner argues (Pet. 16-18) that collateral estoppel should not apply in this case because, if the decision of the court of appeals is allowed to stand, two taxpayers within the same circuit will be treated differently. Petitioner asserts that the taxpayer in *Transwestern Pipeline Co.* v. *United States*, 639 F.2d 679 (Ct. Cl. 1980), will receive tax treatment more favorable than petitioner has received. That contention, which lacks legal merit in any event, is simply factually incorrect. In *Transwestern*, the taxpayer was allowed to depreciate only the *non*recoverable portion of its line pack gas; it was not permitted to depreciate its recoverable gas. See 639 F.2d at 681 (allowing depreciation of "economically unrecoverable gas"); *id.* at 688 (dis-

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in conformity with established law at the time it was entered) is, however, precisely the type of collateral challenge to the prior determination that collateral estoppel does not permit. Only a subsequent change in controlling legal principles may justify an exception from collateral estoppel. See *Montana* v. *United States*, 440 U.S. at 161.

allowing deduction for "recoverable and salvageable" line pack gas). That is identical to the tax treatment afforded to petitioner by the decision below (Pet. App. 5a, 13a).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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